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IN THE

Supreme Court of the United States

OCTOBER TERM 1954

No. 135

ROBERT MAXWELL WATTS, *Petitioner*

v.

UNITED STATES OF AMERICA

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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OCTOBER TERM 1954

No.

ROBERT MAXWELL WATTS, *Petitioner*

v.

UNITED STATES OF AMERICA

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

Petitioner, Robert Maxwell Watts, by his counsel, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Tenth Circuit, affirming the judgment of the United States District Court for the District of Colorado.

OPINIONS BELOW

The District Court wrote no opinion. The opinion of the Court of Appeals (R. 367-372) is not yet reported.

JURISDICTION

The judgment of the Court of Appeals was entered on April 16, 1954 (R. 373). An order staying the mandate

of the Court of Appeals to May 16, 1954, was entered on April 23, 1954 (R. 373). On May 10, 1954, an order was entered by Mr. Justice Clark extending the time for the filing of a petition for a writ of certiorari to June 15, 1954. On May 21, 1954, an order was entered by the Court of Appeals staying its mandate until June 15, 1954. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254.

QUESTIONS PRESENTED

1. (a) In a criminal tax evasion prosecution, where the defense is in large measure based upon honest mistake, advice of counsel, and lack of fraudulent intent, may the trial court refuse to instruct the jury to return a verdict of not guilty if they believe that items assertedly omitted from income were excluded because of a bona fide misconception of law?

(b) In such a case, may the trial court refuse to instruct the jury to return a verdict of not guilty if they find that at the time of filing the questioned return the defendant believed the return to be true or did not know it was false or did not know an additional tax was due and owing?

(c) In such a case, may the trial court instruct the jury, contrary to the instructions requested, that if the jury finds an understatement of income they can "infer, if the amount is large and substantial, that he [the defendant] knew or must have known that he was understating his income."?

2. (a) In a criminal tax evasion prosecution, where the defense is in large measure based upon the contention that the defendant attempted to and did in fact compensate for any omissions of income by understating his deductions so that in fact no additional tax was due, may the trial court refuse to instruct the jury that in order to convict the defendant the Government must prove that

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some tax in addition to what the defendant had already paid is due and owing?

(b) In such a case, may the court instruct the jury that if they find that the defendant did not report a substantial amount of income received, they are required to find as a matter of law that there is an additional amount of tax due and owing the United States?

3. (a) In a criminal tax evasion prosecution based in part on net worth computations, is the Government required to definitely establish the defendant's opening net worth?

(b) In such a case, may the court shift to the defendant either the burden of establishing his opening net worth or the burden of establishing whether or not asserted increases in net worth are derived from taxable income?

4. (a) Where the evidence unequivocally establishes and the prosecution explicitly states that an item of property received by the defendant in an earlier year was received in consideration of services rendered and was taxable, though not reported, in the earlier year, may the trial court, in a criminal tax evasion prosecution, instruct the jury that they can find that the initial value of the property is taxable in a subsequent year in which the property is sold?

(b) Where a taxpayer erroneously deducts the cost of constructing a house, such cost in fact being a capital expenditure, is the taxpayer thereby precluded from capitalizing the cost for the purpose of computing gain in a subsequent year in which the property is sold?

(c) May the court compensate for an understatement of income or an improper deduction in an earlier year by permitting the jury to consider the item as income in a subsequent year in which the taxpayer is charged with tax evasion?

5. Where the trial court specifically calls to the jury's attention the fact of defendant's indictment, may the court refuse to instruct the jury that the indictment is a mere accusation and is not in and of itself any evidence of guilt?

6. In a criminal tax evasion prosecution based entirely on circumstantial evidence, may the trial court refuse to give the jury any instruction whatsoever to the effect that the defendant must be acquitted if the proof is not such as to exclude every reasonable hypothesis other than that of guilt?

7. May the trial court refuse to instruct the jury upon the section of the statute which forms the basis of the indictment?

8. May the trial court instruct the jury that the reasonable doubt which would require a verdict of acquittal in a criminal case is the "kind of doubt" which the jury "*would be willing to act upon* in the[ir] more important affairs", as distinguished from an instruction to the effect that the doubt must be of a kind which would lead the jury *to hesitate to act or refrain from acting?*

STATUTES INVOLVED

Internal Revenue Code:
Sec. 145 (b). Penalties.

> *Failure to collect and pay over tax, or attempt to defeat or evade tax.* Any person required under this chapter to collect, account for, and pay over any tax imposed by this chapter, who willfully fails to collect or truthfully account for and pay over such tax, and any person who willfully attempts in any manner to evade or defeat any tax imposed by this chapter or the payment thereof, shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, be fined not more than $10,000, or imprisoned for not more than five years, or both, together with the costs of prosecution. (26 U. S. C. 1946 ed., Sec. 145 (b)).

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STATEMENT

The facts, insofar as they are relevant to the issues raised in this petition, are as follows: Petitioner, a contractor and builder in the Cities of Pueblo and Craig, Colorado, was convicted of violating Section 145 (b) of the Internal Revenue Code under an indictment charging him with willfully and knowingly attempting to defeat and evade income taxes for the year 1946 by filing a false return stating his income to be $3,116.69 and his tax $404.38, whereas his income was $27,850.81 and his tax $10,704.12 (R. 6, 8, 142). The Government took the position, introducing evidence in support thereof, that the petitioner had neglected to reflect several taxable transactions on his income tax return (R. 129-132). The Court of Appeals stated that "Without analyzing these items in detail, it is sufficient to say that they are of such a nature that many, if not all, constituted income to appellant, depending upon whether the jury believed the Government's version of the evidence or that offered by the appellant." (R. 368).

The largest single item of income asserted to have been omitted related to the receipt by petitioner of 85 shares of stock from the Moffat County State Agency, a corporation, of which petitioner was a substantial stockholder. An obligation of the corporation to petitioner for services previously rendered by petitioner was reduced in the amount of $8,500. upon issuance of the stock (R. 49-50, 154-176). At the time the stock was issued the corporation was heavily in debt and was in fact unable to pay the salaries previously agreed upon for its officers (R. 54-57). The Government's witness on value expressly stated that he was not testifying as to market value (R. 60-62, 124-125, 154-156). Petitioner testified that he did not believe that the stock had any ascertainable value and that both his accountants and an attorney to whom he made full disclosure advised him that the stock was not reportable as income if it had no ascertainable value (R. 55-56, 185-186).

The second largest item involved related to the sale in 1946 of a house described as the 901 Security Street property. In computing his gain petitioner used as a base the sum of $7,003.04, reflecting an initial cost base of $6,000, plus improvements in the amount of $1,003.04 (R. 371). The evidence showed that the petitioner received the property in 1943 from the Pueblo Housing Corporation of which he was a substantial stockholder, in consideration for services rendered (R. 27-28, 30, 44-46). The corporation transferring the property was credited with $6,000. which was previously owed petitioner for his services (R. 44-46, 84). The attorney for the Government stated: "We claim he received this property in 1943. It was income then and it was not reported then or in 1946, the year of sale." (R. 28). The evidence was conflicting and confusing as to whether or not the petitioner, who actually built the house, had deducted any of the construction costs as ordinary deductions in prior years (R. 99-100, 102, 103, 130, 176-177).

With respect to the omission of other items of income, petitioner testified that he realized he had probably omitted specific items of income; that he had no intention of filing a false return; that because of the short period of time remaining between the preparation of the return and the due date he attempted to and did in fact compensate for any omissions of income by deliberately understating his deductions; and that he believed, on the basis of the return filed, he had paid the Government at least as much tax as was due it (R. 134, 148-149). An accountant testified that from an audit of the books, records and cancelled checks of the petitioner, the petitioner had overstated his net taxable income (R. 206).

The Government also attempted to prove an understatement of income on a "net worth" theory. The net worth proof offered by the Government consisted solely of financial statements for the years 1943-1946 filed with a private lending institution (R. 15-16, 19). The statements were admitted over the objection of counsel (R. 16, 138, 163, 168).

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The Government witness testified that he had checked none of the items set forth as assets and liabilities in the statements and he had no knowledge of their correctness (R. 19). Petitioner's unqualified testimony was that there was no correlation between his taxable income and asserted increases shown by the financial statements; that the items on the financial statements did not reflect the cost of the items to him, but rather reflected his view of the current market value; and that therefore they were replete with appreciations in value which had not been realized for income tax purposes (R. 168-171). No evidence was introduced by the Government to establish, apart from the financial statements, the petitioner's opening net worth, or to prove that the asserted increases in net worth shown by the financial statements were in fact not attributable to unrealized appreciation in value, or to other non-taxable sources.

Petitioner requested and the court refused an instruction that the jury should bring in a verdict of not guilty if they believed that the items involved were omitted by petitioner because of a bona fide misconception of law. Petitioner requested and the court refused an instruction that the jury should bring in a verdict of not guilty if they found that petitioner at the time of filing his income tax return believed it to be true or did not know it to be false or did not know an additional tax was due and owing (R. 260). Petitioner requested and the court refused an instruction that willful evasion requires an intentional act or omission as compared to an accidental or inadvertent act and requires a specific intent to conceal an obligation known to exist as compared to a genuine misunderstanding of the requirements of the law (R. 259). Contrary to the requested instructions, the court instructed the jury that if they found an understatement of income they could "infer, if the amount is large and substantial, that he [the defendant] knew or must have known that he was understating his income." (R. 247).

In connection with petitioner's testimony that he had deliberately understated his deductions to compensate for omissions of income, petitioner requested the court to instruct that the Government must establish a tax due and owing in excess of that paid by petitioner, although it need not prove all of the income and tax alleged in the indictment (R. 260). The court refused and, on the contrary, instructed the jury that if they found that petitioner did not report a substantial amount of income received, they were required to find, as a matter of law, that there was an additional amount of tax due and owing the Government (R. 246). With respect to the 901 Security Street property, petitioner requested the court to instruct that if the petitioner received the property in 1943, its receipt was not income in 1946 and must not be considered by the jury for that purpose (R. 263). The court refused, and instructed the jury that if they found that petitioner claimed the cost of building the house as a deduction in an earlier year "as a matter of law he had no cost in the house, or any other basis, and .... the entire value of the house was profit under the income tax law . . ." (R. 249).

With respect to the net worth proof offered by the Government, the court instructed the jury, over an objection, as follows (R. 247):

> ". . . the government claims that if he, during that time, made purchases, spent money, and that sum of money which he spent is substantially in excess of what he reported on his income tax return, and *that that money is not shown to have been inherited or received by him by way of a gift, it is reasonable to infer that he derived the money from earnings, from income,* and if that sum of money is substantially in a sum larger than the amount he had been reporting on his income tax return you, ladies and gentlemen of the jury, are entitled to take that into account.
>
> *"You may infer that the money was income that he didn't report, and you may infer, if the amount is large and substantial, that he knew or must have known that he was understating his income."* (Emphasis added).

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The trial court further while calling the jury's attention to the fact of the indictment, refused to instruct the jury that the indictment was a mere accusation and was no evidence of guilt in and of itself (R. 257). It refused to instruct the jury on the statute which formed the basis of the indictment (R. 259). It refused to instruct the jury that where a criminal case is based upon circumstantial evidence, the evidence must be inconsistent with every reasonable hypothesis other than that of guilt (R. 260-261). It refused to grant petitioner's request for a standard instruction on burden of proof and instructed the jury in this respect in a manner objected to by petitioner (R. 258, 250, Petition, page 21).

REASONS FOR GRANTING THE WRIT

The decision of the Court of Appeals sustaining the conviction of the petitioner under Section 145 (b) of the Internal Revenue Code raises several questions of substantial importance, particularly in the prosecution of tax evasion cases, and is in conflict or inconsistent in principle with numerous decisions of other Courts of Appeals as well as decisions of this Court.

1. The decisions below, insofar as they effectively eliminated the issue of "intent" from a prosecution under Section 145 (b), are squarely in conflict or totally inconsistent in principle with decisions of the United States Courts of Appeals for the Third, Fourth, Fifth, Sixth and Tenth Circuits. *United States* v. *Martell*, 199 F. 2d 670 (CA 3); *Stinnett* v. *United States*, 173 F. 2d 129 (CA 4); *Jones* v. *United States*, 164 F. 2d 398 (CA 5); *Wardlaw* v. *United States*, 203 F. 2d 884 (CA 5); *Hargrove* v. *United States*, 67 F. 2d 820 (CA 5); *Lurding* v. *United States*, 179 F. 2d 419 (CA 6); *Haigler* v. *United States*, 172 F. 2d 986 (CA 10). The decisions below are further inconsistent in principle with the decisions of this Court in *United States* v. *Murdock*, 290 U. S. 389 and *Spies* v. *United States*, 317 U. S. 492.

The largest single item of income asserted by the Government in this case to have been improperly omitted related to the receipt by the petitioner of 85 shares of stock of a closely held corporation which the Government contended constituted taxable income in the amount of $8,500.00 upon receipt.[1] The entire theory of the defense with respect to the stock as expressed by the testimony of the petitioner was that he did not report the value of the stock as income because he did not believe the stock had any ascertainable value; and that he further consulted both his accountants and an attorney to whom he made full disclosure and who advised him that the stock was not reportable as income if it did not have an ascertainable market value (R. 155-156, 185-186).

With respect to the remaining items assertedly omitted from income the petitioner freely admitted that he realized when he filed the return that he probably omitted specific items of income. The theory of the defense was, however, that the defendant had no intention of filing a false return; that because of the short period remaining between the time his return was prepared and the time it was due he attempted to and did in fact compensate for any omissions of income by substantially understating his deductions; and that he believed that on the basis of the return filed he had paid the Government at least as much tax as was due it (R. 134, 148-149). Substantial support for the petitioner's testimony was given in the testimony of an expert accountant who testified that from an audit of the books, records and cancelled checks of the petitioner, the petitioner had overstated his net taxable income (R. 206).

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[1] The Government's theory was that an obligation of the corporation for services previously rendered by the petitioner was reduced upon issuance of the stock. The record is clear, however, that at the time the stock was issued the corporation was heavily in debt, and was in fact unable to pay the salaries of its officers (R. 54-57). The witness who testified for the Government as to the value of the stock specifically stated that he was not testifying as to its market value but only as to its book value (R. 60-62, 124-125, 154-156).

Notwithstanding this state of the record and notwithstanding the fact that the defense was critically hinged to the issue of the petitioner's good faith and lack of wrongful intent, the trial court improperly refused to instruct the jury to return a verdict of not guilty if they believed that items were omitted by the petitioner because of a bona fide misconception of law (R. 260). The trial judge further refused to instruct the jury to return a verdict of not guilty if they found that at the time of the questioned return the petitioner believed the return to be true or did not know it was false or did not know an additional tax was due and owing (R. 260). And, consistently, the trial court also refused to instruct that a willful evasion of the tax requires an intentional act or omission as distinguished from an accidental, inadvertent or innocent one and requires a specific wrongful intent to conceal an obligation known to exist as compared to a genuine misunderstanding of what the law requires or a bona fide belief that certain receipts are not taxable (R. 259). Having improperly refused the requested instructions, the trial court proceeded to instruct the jury that if they found an understatement of income they could (R. 247):

> ". . . . infer, if the amount is large and substantial, that he [the defendant] knew or must have known that he was understating his income."

The position of the trial court as sustained by the Court of Appeals is contrary to the principles enunciated by this Court in the *Spies* and *Murdock* cases, *supra*, and by the Courts of Appeals in the numerous cases cited above.

The following statement of the Court of Appeals for the Sixth Circuit in *Lurding* v. *United States*, *supra*, page 422, is particularly apt:

> ". . . . The Court advised the jury that the best evidence of what a person intended to do by an act is the act itself. Undoubtedly this generalization in many contextual environments is sound. Standing

> alone, however, it may give rise to misunderstanding in the minds of lay jurors. The act here involved is the filing of an inaccurate return. In the complexity of successive tax laws, many thousands of taxpayers do that innocently. Such filing is unlawful, however, only if made wilfully, with knowledge of its falseness and with intent to evade taxes. *There is no presumption that may be drawn from the act itself—both knowledge and wilfulness must be established by independent proof, direct or circumstantial.*" (Emphasis added).

To the same effect are *Hargrove* v. *United States, United States* v. *Martell,* and *Wardlaw* v. *United States, supra,* all involving reversals of convictions under Section 145 (b) because of erroneous instructions or refusals to instruct on the requirement of intent. Both the *Hargrove* and *Martell* cases, *supra,* reiterate the principle that "a specific wrongful intent to conceal an obligation known to exist" is a prerequisite to a conviction;[2] and this intent, as emphasized by the Court of Appeals in the *Wardlaw* case, *supra,* page 885, "is not inherent in the act itself, but ... must be proved by or clearly inferred from the evidence". In the present case the trial court's position, sustained by the Court of Appeals, with respect to the instructions requested and the instruction actually given on the issue of intent was not only erroneous as a matter of law but served to exclude from the jury's consideration a defense of primary importance. As the Court of Appeals for the Fifth Circuit stated in *Jones* v. *United States, supra,* page 400, in dealing with the same problem and in commenting upon the decision of this Court in the *Spies* case, *supra:*

> ".... the Supreme Court, pointing out with admirable clarity and correctness the nature of the accusation pressed in this case and of the evidence required to establish guilt of it, has left in no doubt the right of a defendant so charged to have his defenses clearly and fairly put."

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[2] *United States* v. *Martell, supra,* page 672.

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2. The decisions below, insofar as they effectively eliminated the requirement of proof of an additional tax due and owing to sustain a conviction under Section 145(b), are in conflict or inconsistent in principle with decisions of the United States Courts of Appeals for the Second, Seventh, and Eighth Circuits in *United States* v. *Schenck*, 126 F. 2d 702 (CA 2); *Tinkoff* v. *United States*, 86 F. 2d 868 (CA 7); *United States* v. *Rosenblum*, 176 F. 2d 321 (CA 7); and *Gleckman* v. *United States*, 80 F. 2d 394 (CA 8). As previously indicated, the defense was in large measure based upon the contention that while the petitioner did receive items of income not reflected in his return, he attempted to and did in fact understate his deductions to compensate for omitted items of income so that there was in fact no tax due in excess of that paid in accordance with the questioned return. The petitioner's testimony to this effect was supported by the expert testimony of an accountant who testified from the books and records of the petitioner that no additional tax was due in excess of that paid by the petitioner (R. 206). In this state of the record the petitioner requested the court to instruct the jury that in order to convict the petitioner the Government must establish "that a tax, in addition to what the defendant has already paid is due and owing . . . although the Government need not prove all of the income and tax alleged in the indictment". (R. 260). The trial court refused to grant the requested charge to which the petitioner was clearly entitled under the decisions recited above. Contrary to the requested instruction the trial court instructed the jury that "the tax follows as a matter of law from a determination of whatever income was earned which should have been reported." (R. 246). The court further instructed the jury as follows (R. 246):

> ". . . . if you find that the defendant had substantial taxable income in the year 1946 which he did not report on his income tax returns, then you will find that there was a substantial amount of tax due to the United States Government for that year . . ."

The effect of the rulings of the trial court as sustained by the Court of Appeals was not only to mislead the jury as to the requirement of proof of an additional tax due and owing to sustain a conviction, but further to exclude from the jury's consideration a complete defense, namely, that while the petitioner may have understated his income his deductions were similarly understated so that no tax was due the United States in excess of that paid in accordance with the return. The effect of the court's instructions here when considered with relation to the instructions on intent was to exclude the entire theory of the defense from the jury's consideration.

3. The decisions below, insofar as they relate to the Government's net worth proof, which was based solely on petitioner's financial statements, and to the trial court's instructions imposing upon the petitioner the burden of proving that asserted increases in net worth were not attributable to taxable income, are in conflict or inconsistent in principle with decisions of the United States Courts of Appeals for the Third, Fifth, Seventh, and Ninth Circuits. *United States* v. *Caserta*, 199 F. 2d 905 (CA 3); *Ford* v. *United States*, 210 F. 2d 313 (CA 5); *Bryan* v. *United States*, 175 F. 2d 223 (CA 5); *United States* v. *Fenwick*, 177 F. 2d 488 (CA 7); *Olender* v. *United States*, 210 F. 2d 795 (CA 9); and *United States* v. *Calderon*, 207 F. 2d 277 (CA 9) cert. granted June 7, 1954, 22 L. W. 3321. The importance of these net worth questions has been recognized recently by this Court when on June 7, 1954, it granted certiorari in *Holland* v. *United States*, No. 650; *United States* v. *Calderon*, No. 577; *Smith* v. *United States*, No. 726; and *Friedberg* v. *United States*, No. 510; 22 L. W. 3321; all involving the same fundamental net worth questions. The decisions below violate the fundamental principles enunciated by the Courts of Appeals for the Third, Fifth, Seventh, and Ninth Circuits, *supra*, holding that the Government has the burden of proving with definiteness and by credible evidence (a) the defendant's opening net

worth; (b) the fact that defendant's net worth has increased in the tax year involved; and (c) the fact that such increase in net worth is attributable to taxable income. In the present case the net worth proof offered by the Government consisted solely of financial statements for the years 1943-1946 filed by the petitioner with a private lending institution. The Government's agents admittedly checked none of the items set forth as assets and liabilities on the statements and had no knowledge of the correctness of any of these items (R. 19). The petitioner's unqualified and undisputed testimony was that there was no correlation between his taxable income and the asserted increases shown by the financial statements; that the items on the financial statements did not reflect their cost to him but rather reflected his view of the current market value; and that, therefore, they were replete with appreciations in value which had not been realized for income tax purposes (R. 168-171). No evidence was introduced by the Government to refute this testimony. No evidence was introduced by the Government to prove that the asserted increases shown by the financial statements were in fact not attributable to unrealized appreciation in value, or to other nontaxable sources such as gifts or inheritance. Under these circumstances, it was patent error for the trial court to overrule the objections to the admission of this evidence which were continually pressed during the trial (R. 16, 138, 163, 168). The trial court not only failed to instruct the jury to ignore the net worth evidence, but proceeded to instruct the jury erroneously as follows (R. 247):

> " . . . . the government claims that if he, during that time, made purchases, spent money, and that sum of money which he spent is substantially in excess of what he reported on his income tax return, *and that that money is not shown to have been inherited or received by him by way of a gift, it is reasonable to infer that he derived the money from earnings, from income, and if that sum of money is substantially in a sum larger than the amount he had been report-*

ing on his income tax return you, ladies and gentlemen of the jury, are entitled to take that into account.

"*You may infer that the money was income that he didn't report, and you may infer, if the amount is large and substantial, that he knew or must have known that he was understating his income.*" (Emphasis added).

Thus the trial court compounded its original error of permitting the jury to consider financial statements which proved nothing about taxable income, by imposing upon the petitioner the burden of proving that the asserted increases in his net worth were not attributable to taxable income and by instructing the jury that they might infer that the increases reflected unreported income. The conflict with the principles adhered to in the decisions above is irrefutable. As the Court of Appeals said in *Ford* v. *United States, supra* (page 315):

" . . . . One of the most difficult matters of proof in such cases is to establish a satisfactory starting point at the beginning of the first of the tax periods included in the indictment, that is as applied to the present case, to negative the existence on January 1, 1945, of resources available to the defendant and his wife from which the excessive expenditures might have come. *The Government then has the further burden in such cases of proving that there were no gifts, devices, or other nontaxable income which could have been used for the expenditures, and of proving large cash expenditures within each of the tax years considerably exceeding the taxpayer's accumulated cash resources plus reported income and which expenditures could not be otherwise accounted for than by finding that the taxpayer had received more taxable income than had been reported,* and had willfully and knowingly filed or caused to be filed a false and fraudulent income tax return." (Emphasis added).

While the present petition involves several other questions of great importance, the net worth questions presented

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here are alone of sufficient importance to require this Court's consideration.

4. The decisions below, insofar as they allowed the jury to compensate for an understatement of income or an improper deduction in an earlier year by considering the item as income in a subsequent year in which the taxpayer was charged with tax evasion, are in derogation of the annual accounting concept of the Internal Revenue Code and are in conflict or inconsistent in principle with decisions of the United States Courts of Appeals for the First, Third, Fourth and Eighth Circuits. *Ross* v. *Commissioner of Internal Revenue*, 169 F. 2d 483 (CA 1); *Commissioner of Internal Revenue* v. *Mellon*, 184 F. 2d 157 (CA 3); *Clifton Mfg. Co.* v. *Commissioner of Internal Revenue*, 137 F. 2d 290 (CA 4); *Greenwood Packing Plant* v. *Commissioner of Internal Revenue*, 131 F. 2d 787 (CA 4); *Welp* v. *United States*, 201 F. 2d 128 (CA 8). The unequivocal evidence established that in 1943 the petitioner received from the Pueblo Housing Corporation a piece of property described as 901 Security Street in consideration for services rendered (R. 27-28, 30, 44, 46). The evidence also unequivocally established that the corporation transferring the house was credited in 1943 with $6,000.00 which was previously owed by it to the defendant (R. 44, 46, 184). The house was thus taxable income in 1943, the year of its receipt by the petitioner, and this was precisely the theory of the prosecution. Thus, the attorney for the Government made the following statement: "We claim he received this property in 1943. It was income then and it was not reported then or in 1946, the year of sale." (R. 28). In this factual context the petitioner requested the court to instruct the jury (R. 263):

> ". . . that if the Pueblo Housing Corporation conveyed the property located at 901 Security Street in the City of Pueblo to the defendant during the year 1943, the receipt of the property was not income during the year 1946, was not reportable as such and must not be considered by you for that purpose."

The instruction was refused (R. 263). That the petitioner, under the annual accounting concept of the federal revenue laws, was entitled to such an instruction is clearly established by the decisions of the Courts of Appeals in the above-cited cases. As the Court of Appeals for the First Circuit in *Ross* v. *Commissioner of Internal Revenue, supra*, stated, page 492:

> ". . . a taxpayer has an affirmative obligation to report any income falling within its scope in his return for the year of such receipt, and that his failure to do so will subject him to such liabilities for interest, penalties, or even criminal prosecutions, as may be appropriate to his case. If this is so, the doctrine does not merely afford a special choice which the Commissioner may, if he sees fit, exercise retroactively against a taxpayer, but a rule of law determining what constitutes taxable income, and as such presumably binding on all parties."[3]

Contrary to and in disregard of the settled rule, the trial court erroneously instructed the jury that if they found that the petitioner claimed the cost of building the house as a deduction in a prior year "as a matter of law he had no cost in the house, or any other basis, and . . . the entire

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[3] The court after rejecting a defense of estoppel by pointing out that "A mere failure to report income is not a representation that such income has in fact not been received", went on to observe, page 496:

> "In sum, we hold that the Tax Court, erred in attributing to 1939 the disputed items of accrued salary, that if these items were constructively received when earned they cannot be treated as income in any later year, that the doctrine of election is inapplicable to the facts of this case, and, in the absence of misstatement of fact, intentional or otherwise, the petitioner cannot be estopped from asserting that the items were taxable only in the years in which constructively received."

To be noted also are the provisions of Section 3801 of the Internal Revenue Code which would permit a readjustment of the petitioner's liability for the earlier year in which there was an erroneous exclusion from income or erroneous deduction.

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value of the house was profit under the income tax law . . ." (R. 249). The Court of Appeals without citation of authority adopted this view, which was in fact wholly wrong under the very same principle of law expressed in the previously cited cases. Construction costs are capital expenditures and not ordinary deductions; and the Government could no more compensate for an erroneous deduction in a prior year than it could for an understatement of income. Being capital expenditures, the construction costs formed part of the petitioner's base whether or not he erroneously deducted any such costs in a prior year. The law on this precise point is well summed up in *Mertens' Law of Federal Income Taxation*, Vol. 4, Section 23.26, page 31, where the author states:

> "CAPITALIZATION OF ASSETS PREVIOUSLY ERRONEOUSLY CHARGED OFF AS EXPENSE. If, by reason of inadvertance or irregular accounting practices, capital investments have been charged off as expense items, they may be restored and depreciation allowed on such capital investment. It has been said:
>
> > 'The mere failure of a taxpayer to take the proper deduction in each year does not permit him to take advantage of his mistake through an incorrect return in a later year nor does it permit the Commissioner to compel an incorrect return. The law does not contemplate the adjustment in any part of an incorrectly computed tax by the incorrect computation of another tax. . . .'"

5. The decision of the Court of Appeals in sustaining the trial court's refusal to instruct the jury that the indictment was a mere accusation and was not evidence of guilt is squarely in conflict with decisions of the United States Courts of Appeals for the Third, Fifth, and Eighth Circuits. *United States* v. *Schanerman*, 150 F. 2d 941 (CA 3); *Gold* v. *United States*, 102 F. 2d 350 (CA 3); *Patterson* v. *United States*, 183 F. 2d 687 (CA 5), cert. denied 343 U. S. 951; *Cooper* v. *United States*, 9 F. 2d 216 (CA 8); *Nanfito*

v. *United States,* 20 F. 2d 376 (CA 8). Nor is there any merit whatsoever in the suggestion of the Court of Appeals that the need for such an instruction can be obviated by an instruction on burden of proof or presumption of innocence. An instruction relating to the requirement that the Government adduce evidence which convinces the jury beyond a reasonable doubt or to the presumption that a man is innocent until such evidence is produced has no bearing on the question as to whether or not an indictment may be considered as evidence by the jury. Nor can any support be found for the court's position in the decisions of the other Courts of Appeals cited above. Particularly where, as here, the trial court in its instruction calls to the jury's attention the fact that a defendant has been indicted and has been charged with a criminal offense, it is all the more important that the trial court instruct the jury that the indictment has no evidential significance.

6. The decisions below raise, in addition to Question 3, three other important questions (6, 7 and 8) which were raised in *Holland* v. *United States,* No. 650, cert. granted June 7, 1954. These questions which stem from the instructions of the trial judge, who is the same judge who presided in the *Holland* case, are set forth in summary form as follows:

(a) As in the *Holland* case, the decisions below are in conflict with decisions of the Courts of Appeals for the Fifth, Sixth, Seventh, and Eighth Circuits holding or acknowledging the principle that where a criminal case is based entirely upon circumstantial evidence, the trial court is required to give some form of instruction to the general effect that the evidence must be inconsistent with every reasonable hypothesis but that of guilt. *Garst* v. *United States,* 180 Fed. 339, 343 (CA 4); *Stutz* v. *United States,* 47 F. 2d 1029 (CA 5); *Anderson* v. *United States,* 30 F. 2d 485, 487 (CA 5); *Bryan* v. *United States, supra,* page 226; *Strickland* v. *United States,* 155 F. 2d 167, 168 (CA 5);

McLendon v. *United States*, 13 F. 2d 777, 779 (CA 6); *Epstein* v. *United States*, 174 F. 2d 754, 769 (CA 6); *United States* v. *Fenwick*, 177 F. 2d 488, 490 (CA 7); *Gurera* v. *United States*, 40 F. 2d 338, 340 (CA 8); *Banks* v. *United States*, 204 F. 2d 666, 672 (CA 8).

(b) The decisions below are further in conflict with decisions of the Courts of Appeals for the Third and Ninth Circuits holding, contrary to the decision here, that the trial court is required to instruct the jury with respect to the statute governing the offense and not merely as to the factual elements set forth in the indictment. *United States* v. *Pincourt*, 159 F. 2d 917 (CA 3); *United States* v. *Levy*, 153 F. 2d 995 (CA 3); *United States* v. *Noble*, 155 F. 2d 315 (CA 3); *Morris* v. *United States*, 156 F. 2d 525 (CA 9).

(c) The decision below upholding an instruction on reasonable doubt as the "kind of doubt" the jury "*would be willing to act upon* in their more important affairs" (R. 250) is in conflict with every State court appellate decision in which such instruction has been considered. *Commonwealth* v. *Miller*, 139 Pa. 77, 21 Atl. 138; *State* v. *Rover*, 11 Nev. 343; *People* v. *Bemmerly*, 87 Cal. 117, 25 Pac. 266; *Lovett* v. *State*, 30 Fla. 142, 11 So. 550, all to the effect that reasonable doubt is that doubt which would lead reasonable men to *refrain from acting* or *hesitate to act*, rather than the converse set forth in the instructions here.

CONCLUSION

The questions raised in this petition are of great importance in the proper administration of the revenue as well as the criminal laws and they are of particular importance in the proper construction and application of Section 145 (b) of the Internal Revenue Code. Petitioner desires to stress that entirely apart from those questions, particularly the net worth questions, which are common to this case and to other cases in which this Court has recently

granted certiorari, additional questions are here presented of such importance as to independently warrant consideration by this Court.

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